Supreme Court, U.S.
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No. 04 191

In The
Supreme Court of the United States

COLE SMITH,

Petitioner

v.

RUSH RETAIL CENTERS, INC.,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

1. Does the need for a uniform national policy regulating employment arbitration agreements under the Federal Arbitration Act, as expressed in *Circuit City Stores v. Adams*, create a "federal question," giving Federal Courts jurisdiction to enforce and oversee all such agreements?

2. Can a uniform national policy governing employment arbitration agreements be achieved if only State Courts have jurisdiction to interpret and apply the Federal Arbitration Act to some employment arbitration agreements?

3. Does the Federal Arbitration Act, as interpreted in *Circuit City Stores v. Adams*, grant Federal Courts jurisdiction of all employment arbitration agreements?

LIST OF PARTIES

1. Cole Smith, Petitioner

2. Rush Retail Centers, Inc.

3. Rush Enterprises, Inc., a publicly held parent company

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IN THE SUPREME COURT OF THE UNITED STATES

COLE SMITH, *Petitioner*,

v.

RUSH RETAIL CENTERS, INC., *Respondent.*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The Petitioner Cole Smith respectfully prays that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit, entered in the above-entitled proceeding on March 3, 2004.

OPINIONS BELOW

The opinion of the District Court is reported as 291 F.Supp. 2d 497. The opinion of the Court of Appeals for the Fifth Circuit is reported as 360 F.3d 504.

GROUNDS FOR JURISDICTION

Petitioner invoked jurisdiction in the District Court under the Federal Arbitration Act 9 U.S.C. §10 and under 28 U.S.C. §1331. The District Court denied federal jurisdiction in an Opinion dated July

1, 2003 and denied Petitioner's Motion for Rehearing on July 25, 2003. Petitioner appealed to the Fifth Circuit Court of Appeals, which affirmed (on March 3, 2004) the District Court's Ruling that the Federal Arbitration Act (FAA) does not grant Federal jurisdiction and that same exists only when there is diversity of citizenship or a Federal question involved. Petitioner Smith and Respondent are both citizens of Texas and Smith alleged only a violation of the employment contract itself. Pursuant to the Court's recent interpretation of the FAA in *Circuit City Stores v. Adams*, 121 S. Ct. 1302 (2001) (holding that the FAA pre-empts state employment arbitration statutes) Smith says that a "Federal question" is involved, which creates Federal jurisdiction. This Court has jurisdiction under 28 U.S.C. §1254(1).

STATUTE INVOLVED

9 U.S.C. §10 provides: "(a) In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration –

(3) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced."

STATEMENT OF THE CASE

The facts relevant to the jurisdiction issue are undisputed. Smith and Respondent executed an Employment Agreement calling for arbitration of all employment disputes. It also specified that the FAA and the Federal Rules of Civil Procedure would apply. Smith was terminated and proceeded to arbitrate his claim that the Respondent breached the contract in various fashions. The Arbitrator ruled against Smith and he timely filed suit in Federal District Court in San Antonio (as specified by Section 10b of the FAA) seeking to set aside the award. Smith alleged that the Arbitrator had committed misconduct under Section 10 of the Statute and, additionally had violated the non-statutory standard, developed by the Federal Courts, that an arbitration award can be set aside when the Arbitrator engages in "manifest disregard of the law".

Smith pleaded that the Federal Court had jurisdiction under the FAA and that a federal question was also raised which created jurisdiction under 28 USC §1331. The district court referred the matter to a Magistrate Judge who found that the Federal courts had no jurisdiction under the FAA to set aside the award. The District court entered an Opinion adopting such recommendation. The 5th Circuit Court of Appeals affirmed that decision. This case presents the question of whether the Federal courts have jurisdiction to carry out the purpose of the FAA, as envisioned by the Court in *Circuit City Stores*, *supra*.

REASONS FOR GRANTING THE WRIT

For the last 47 years this Court has consistently ruled that arbitration of employment disputes under Collective Bargaining Agreements ("CBAs") are governed by Federal substantive law to be applied exclusively by Federal courts. This consistent approach was not easily discerned from the sparse provisions of the Labor Management Relations Act 29 USC §185, and many landmark decisions were required before all the applicable principles were fully developed.[1] The theme in all of such litigation was solidly based upon the need for a uniform national policy toward Arbitration of disputes under these agreements, which was to be developed exclusively in the Federal courts. The same theme (and jurisdiction) must be developed and applied with regard to individual employment agreements under the FAA for the same reasons.

In contrast to the long history of enforcement of Arbitration provisions in CBAs, the enforcement and regulation of individual employment arbitration agreements is in its infancy. Its history began with the decision of this Court in *Circuit City Stores*, in the year 2001, where the Court held that the FAA governs such agreements and pre-empted contrary state laws. The present case presents, for the first

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[1] *Textile Workers Union v. Lincoln Mills of ALA.*, 77 S.Ct. 912 (1957); *United Steelworkers of America v. Warrior and Gulf Nav. Co.*, 80 S.Ct. 1347 (1960); *Lingle v. Norge Division of Magic Chef, Inc.*, 108 S.Ct. 1877 (1988); *United Assn. Of Journeyman Etc. v. Local 334*, 101 S.Ct. 2546 (1981).

time, the question of whether the same concern for a uniform national policy regarding arbitration of individual employment agreements will prevail. Absent jurisdiction in the Federal Courts, 50 different state courts will imprint their interpretations on the FAA in those frequent instances where a Federal statute is not involved and there is no diversity of the parties.

In *Circuit City Stores* the Court held that, in spite of apparent limiting language contained in Section 1 of the FAA, there was a clear need for uniform regulation of individual arbitration agreements, and thus the FAA governed all such agreements[2]. Twenty-two states filed Amicus Briefs urging the Court to allow their individual state statutes to govern such agreements. In finding that the FAA pre-empted all such state statutes this Court stated that such a patchwork system of regulation by the states would lead to many conflicts and complications, which would result in additional litigation – thus causing the resulting delay and costs of arbitration to outweigh its benefits! It was pointed out that this was particularly true for the many multi-state employers who had such arbitration agreements in place. *Circuit City Stores*, p. 1313.

If allowed to stand, the ruling that Federal Courts have jurisdiction to apply the FAA in only limited cases will create precisely the same evils as the Court sought to avoid by its decision in *Circuit City Stores*. There are many employment arbitration

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[2] Where Interstate Commerce was involved.

disputes that do not implicate Federal statutes and where the parties are not diverse. It is submitted that there is no diversity in most employment disputes. Likewise, many disputes do not involve Federal statutes. To foreclose the Federal Courts from applying and interpreting the FAA in those instances will force many of the issues concerning the arbitration process and the review thereof, (presently unresolved) to be developed in the various state courts. The courts of each state, in attempting to apply the FAA, will naturally develop their own interpretation of it. Invariably these decisions will also conflict with the Federal Courts' own interpretation of the FAA in those cases where they have jurisdiction. The provisions of the FAA are very sketchy, and an incredible number of issues remain to be "fleshed out".

By way of illustration, some such issues (but not all) are as follows:

1. Is an arbitration agreement valid that requires the employee to pay half of the cost of arbitration?

2. Are arbitration agreements valid which contain limitations on the damages or other remedies that an arbitrator can award?

3. Are agreements valid that contain substantial restrictions on an employee's ability to engage in discovery?

4. Are agreements valid that contain venue requirements that substantially disadvantage the employee?

5. Are agreements valid that call for arbitrators to be appointed by unknown (and perhaps bias) arbitration organizations? (Organizations that actively solicit employers to use their arbitrators).

6. If the award is set aside, what are the standards for deciding if the case should be sent back to the same arbitrator or sent to a new arbitrator?[3]

The Federal Courts have begun to deal with some of these issues, on the road to developing a uniform national policy under FAA. For example, s*ee Morrison v. Circuit City Stores, Inc.*, 317 F.3d 646 (6th Cir. 2003).

The FAA contains nothing that attempts to answer these questions (and many other similar questions that will develop). It was passed in 1925 with its principle purpose being to simply get the Courts to recognize the validity and usefulness of the arbitration process. Arbitration and Alternative Dispute Resolution ("ADR") have come a long way since then. Now arbitration and ADR are specifically endorsed by some Federal employment

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[3] These agreements are drafted by the employer and the employee must take it or leave it, as written.

statutes, such as the Americans with Disabilities Act. 42 U.S.C. § 12212.

In one major area, where the FAA is lacking, the Federal Courts have been diligent in developing a test for reviewing arbitration awards. They have established a non-statutory standard that an arbitrator's decision will not be enforced where the arbitrator engaged in "manifest disregard of the law." *Williams v. Cigna Financial Advisors*, 197 F.3d 752 (5th Cir. 1999); *Greenberg v. Bear Sterns & Co.*, 220 F.3d 22 (2nd Cir. 2000). This is an area totally unfamiliar to most state courts. In doing this "gap filling" of the FAA's provisions, each state may well be influenced by the provisions of the its own arbitration statutes. Clearly there are 22 states whose statutes are adverse to some of the provisions of the FAA. In developing their own versions of the FAA these states may regain some of the ground they lost in *Circuit City Stores.*

Prior to *Circuit City Stores* and consistent with it, in *Allied-Bruce Terminix Companies, Inc. v. Dobson*, 115 S.Ct. 834 (1995), the Court addressed an attempt to carve out a "nitch" in the FAA in which States could regulate employment arbitration agreements. The Court replied:

> "We must decide in this case whether that Act (the FAA) used language about interstate commerce that nonetheless limits the Act's application, thereby carving out an

> important statutory niche in which a State remains free to apply its antiarbitration law or policy. We conclude that it does not." *Allied-Bruce*, 115 S. Ct. at 839.

The lesson learned from the litigation over arbitration clauses under CBAs is that uniformity can only come through the Federal courts. The Court recognized this in *Circuit City Stores* when it referred to the pre-emption of ERISA, citing the Court's same day decision of *Egelhoff v. Egelhoff,* 121 S.Ct. 1322 (2001) (p. 1313).

It is interesting that the Court's first case that announced the need for a uniform national policy regarding arbitration of employment disputes under CBAs was a mirror image of the present case. *Textile Workers*, *supra note 1*. There the statute granted jurisdiction, but was totally silent on what substantive law governed. Here the Court has declared that the FAA provides the substantive law and the question is, will jurisdiction be found in order to apply it. To obtain a uniform national policy the Court, in *Textile Workers*, read the statute broadly to determine that a federal substantive law needed to be developed to accomplish the statutory purpose. The same approach must apply regarding the present jurisdiction issue, if uniformity is to be achieved! In *Circuit City Stores*, the Court again read the applicable statute broadly to accomplish the same purpose as expressed in *Textile Workers* and concluded that it pre-empted state employment arbitration laws. Complete pre-emption by the FAA

of these type agreements clearly creates Federal jurisdiction. *Caterpillar v. Williams*, 107 S.Ct. 2425 (1987) p. 2430.

CONCLUSION

The clear message of *Circuit City Stores*, was that the FAA pre-empted state employment arbitration statutes. This result was founded on the need for uniformity across the nation – the same theme consistently followed for employment arbitration under CBAs for 47 years. Federal jurisdiction over all individual employment arbitration agreements (without regard for diversity or allegations of a Federal statutory violation) is the only route to achieve uniform interpretation and enforcement of the FAA and to continue to encourage the arbitration of individual employment disputes.

Respectfully submitted,

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APPENDIX

A. Report and Recommendation of U.S. Magistrate Judge, dated June 6, 2003.

B. Order Accepting Report and Recommendation of the United States Magistrate Judge for the Western District

of Texas – San Antonio Division, dated July 1, 2003. 291 F.Supp. 2d 479

C. Order Denying Plaintiff's Motion for Rehearing and to Amend Judgment, dated July 25, 2003.

D. Opinion for the United States Court of Appeals for the Fifth Circuit dated March 3, 2004. 360 F.3d 504

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

COLE SMITH,	§	
	§	
Plaintiff,	§	
	§	
v.	§	No. SA-02A-1022
	§	
RUSH RETAIL CLEANERS,	§	
	§	
	§	
Defendant.	§	

REPORT AND RECOMMENDATION
DATED JUNE 6, 2003

MATHY, United States Magistrate Judge.

Honorable Fred Biery United States District Judge.

Pursuant to the order of referral in the above-styled and numbered cause of action to the undersigned United States Magistrate Judge [FN1] and consistent with the authority vested in United States Magistrate Judges under the provisions of 28 U.S.C. § 636(b)(1)(B) and rule

1(d) of the Local Rules for the Assignment of Duties to United States Magistrate Judges in the Western District of Texas, effective January 1, 1994, the following report and recommendation is submitted for your review and consideration.

FN1. Docket no. 14.

I. *JURISDICTION*

Plaintiff's complaint alleges jurisdiction pursuant to 9 U.S.C. § 10 and 28 U.S.C. § 1331.

II. *PROCEDURAL HISTORY*

This case was initiated on October 21, 2002, when plaintiff Cole Smith ("Smith") filed an original complaint against Rush Retail Centers, Inc. ("Rush") seeking to vacate an arbitration award. [FN2] In brief, Smith alleged he sold his business to Rush, and, as a part of the transaction, entered into a five-year employment contract. Thereafter, Rush terminated Smith's employment. Pursuant to the arbitration clause of the employment contract, Rush requested arbitration to resolve his objection to his termination. Arbitration was conducted in San Antonio, Texas and the arbitration panel [FN3] entered a decision denying recovery to Smith. Thereafter, plaintiff filed this lawsuit seeking an order requiring the retrial of the case before a different arbitration

panel, or, alternatively, an order requiring retrial before the same *482 arbitration panel, but with provisions in the order to provide specific instructions as to how the employment contract should be interpreted, "that relevant evidence be admitted and considered," and that "applicable Texas law be applied to the interpretation" of the employment contract. [FN4] Plaintiff also seeks recovery of "all costs incurred." [FN5] Plaintiff filed an appendix to his complaint consisting of the transcript of record before the arbitrators, exhibits offered, the arbitration decision, and post-arbitration hearing pleadings. [FN6]

FN2. Docket no. 1.

FN3. Although plaintiff's complaint refers to "the Arbitrator," the final arbitration decision indicates that a panel of three arbitrators heard the dispute and two arbitrators agreed in the decision. *Id.,* exhibit 6 at 1 and 9. Accordingly, this report refers to "arbitrators" or the arbitration panel.

FN4. *Id.* at 3.

FN5. *Id.*

FN6. Specifically, the appendix consists of six documents, marked as exhibit 1 through 6, respectively: plaintiff's post-hearing brief, Rush's post hearing brief, plaintiff's motion for reconsideration of excluded evidence, Rush's response, the arbitration panel's order denying reconsideration, and the final decision of the arbitration panel, captioned "binding arbitration decision and opinion." In support of his complaint, plaintiff also has tendered the transcript of record and notebooks containing the exhibits offered during the arbitration proceedings. *See* docket no. 1, Affidavit of Durwood D. Crawford, and attachments.

On December 3, 2002, defendant filed its answer to the complaint which included a counterclaim seeking enforcement of the arbitration award and an award of attorney's fees and costs. [FN7] Specifically, defendant asserted "[p]laintiff was contractually prohibited from seeking vacatur of the arbitration award. Plaintiff has breached this contract, thereby entitling defendant to attorney's fees." [FN8]

FN7. Docket no. 2.

FN8. Docket no. 2 at 3.

On December 20, 2002, plaintiff filed a brief in support of his petition to vacate the arbitration award. [FN9] On January 17, 2003, Rush filed a brief in response. [FN10] On February 3, 2003, plaintiff filed a reply brief. [FN11] Rush filed a sur-reply on March 18, 2003, [FN12] a sur-response on May 20, 2003, [FN13] and Smith filed a sur-response to Rush's sur-response on May 20, 2003. [FN14] On or about May 20, 2003, this case was referred to the undersigned.

FN9. Docket no. 5. An attachment to the brief consists of excerpts from the arbitration record.

FN10. Docket no. 6. Defendant attached four exhibits to his response, marked as exhibits A through D, respectively: the employment agreement in question; the July 13, 2001 letter terminating plaintiff's employment; resumes of the three arbitrators; and the "binding arbitration decision and opinion."

FN11. Docket no. 7.

FN12. Docket no. 10.

FN13. Docket no. 12.

FN14. Docket no. 13.

III. *STATEMENT OF THE CASE*

On September 1, 2000, the parties entered into a five-year written employment agreement. [FN15] The employment agreement contains the following two provisions which relate to the termination of plaintiff's employment: [FN16]

FN15. Docket no. 1 at 2; docket no. 6, exhibit A.

FN16. The employment agreement also contains a provision for "termination by the company without cause," which appears to require defendant to pay plaintiff his monthly base salary of approximately $7,084, through the remainder of the term of the agreement, as well as benefits. Docket no. 6, exhibit A at 3, § 4.1.

4.2 *Termination For Cause.* This Agreement may be terminated by the Company for "Cause" (as defined in Section 8.2 herein) upon written notice *483 thereof given by the Company to Employee .... [FN17]

FN17. *Id.*, exhibit A at 4, § 4.2. Unlike termination by the company
without cause, termination for cause obligated the company to pay plaintiff his monthly base salary, subject to standard deductions, earned *pro rata* to the date of termination. *Id.*

* * * * * *

8.2 "*Cause* " shall be exclusively limited to the following, as determined by the Board in its sole judgment: (i) Employee breaches any material terms of this Agreement; (ii) Employee is convicted of a felony; (iii) Employee fails, after a least one warning, to perform duties assigned under this Agreement (other than a failure due to death or physical or mental disability); (iv) Employee intentionally engages in conduct which is demonstrably and materially injurious to the Company; (v) Employee commits fraud or theft of personal or Company property from Company premises; (vi) Employee falsifies Company documents or records; (vii) Employee engages in acts of gross carelessness or willful negligence to endanger life or property on Company premises; (viii) Employee uses, distributes, or is under the influence of illegal drugs, alcohol, or other intoxicant on Company premises; (ix) Employee possesses or stores hand guns or Company premises; or (x) Employee intentionally violates state, federal or local laws and regulations in the course and scope of his employment. [FN18]

FN18. *Id.*, exhibit A at 7, § 8.2.

On July 13, 2001, plaintiff was notified by letter that his employment was terminated

immediately. [FN19] The letter was signed by Robin M. Rush, defendant's vice president, and provided, in sum, that the termination was due to

FN19. Docket no. 6, exhibit B.

repeated failure to complete assigned and required position duties after warning and notice; deficient managerial skills; abrasive and abusive disrespect when dealing with your employees; actions or lack of actions which endanger the assets and employees of the company; disregard of direct instructions from you superiors and attempting to deceive them following such disregard[.] [FN20]

FN20. *Id.*, exhibit B at 1.

The three-page letter also included information of specific instances of alleged transgressions in support of the decision to terminate. [FN21]

FN21. *Id.*, exhibit B at 1-3.

Plaintiff contested his termination. After informal dispute resolution techniques failed to resolve the dispute, the parties submitted their dispute to binding arbitration in accordance with the arbitration clause of the employment agreement. Article 7 of the employment agreement states:

Except for the provisions of Articles 5 and 6 of this Agreement dealing with proprietary property, confidential information and restrictive covenants, with respect to which the Company expressly reserves the right to petition a court directly for injunctive and other relief, any claim, dispute or controversy of any nature whatsoever, including but not limited to tort claims or contract disputes between the parties to this Agreement or their respective heirs, executors, administrators, legal representatives, successors and assigns, as applicable, arising out of related to Employee's employment or the terms and conditions of this Agreement, including the implementation, applicability or interpretation thereof, shall be resolved *484 in accordance with the dispute resolution procedures set forth in Appendix A attached hereto and made a part hereof. [FN22]

FN22. *Id.,* exhibit A at 6, Article 7.

Appendix A, in turn, includes three pages of "Dispute Resolution Procedures," which, in sum, requires good faith negotiations within 45 days, and, if informal negotiations do not settle the dispute, for "binding arbitration." [FN23] The agreement also provides: "This arbitration provision shall be government by, and all rights and obligations specifically enforceable under

and pursuant to, the Federal Arbitration Act (9 U.S.C. § 1, *et seq.*)." [FN24]

FN23. *Id.,* exhibit A, appendix A at A-1, §§ B and D.

FN24. *Id.,* exhibit A, appendix A at A-3, § D(8).

Arbitration hearings were held on May 14, 15, and 16, 2002 in San Antonio, Texas before a panel of three arbitrators, one selected by plaintiff, one selected by defendant, and "the third selected by the two arbitrators so selected." [FN25] Both sides were represented by counsel. After hearing extensive testimony reflected in an arbitration hearing transcript of 1,004 pages and admitting into evidence "[i]n excess of one hundred twenty-one (121) rather voluminous exhibits" on behalf of both parties, [FN26] the arbitrators found that plaintiff's employment had been validly terminated for cause. [FN27] More specifically, the arbitrators found plaintiff had "failed to prove by a preponderance of the evidence that Respondent violated the Employment Agreement, and particularly Sections 4.2 or 8.2 thereof." [FN28] The arbitrators explained that:

FN25. *Id.* exhibit D at 1; docket no. 1, exhibit 6 at 1; *see also* docket no. 6, exhibit A, appendix A at A-1, § D(1).

FN26. Docket no. 6, exhibit D at 2.

FN27. Two arbitrators concurred in the result; one arbitrator disagreed. Docket no. 6, exhibit D at 9; docket no. 1, exhibit 6 at 9.

FN28. Docket no. 6, exhibit D at 4; docket no. 1, exhibit 6 at 9.

the Official Record is replete with examples of conduct acts and omissions by Claimant establishing that:
a) Claimant, after at least one warning, failed to perform duties assigned under the Employment Agreement;
b) Claimant engaged in at least one act of gross carelessness or willful negligence endangering life or property; and
c) Claimant intentionally engaged in conduct that is demonstrably and materially injurious to the Company [Respondent]. [FN29]

FN29. Docket no. 6, exhibit D at 4; docket no. 1, exhibit 6 at 4.

The arbitrators found that: section 4.2 of the employment agreement provided that "the Company" could terminate plaintiff's employment for cause, "the Company" had "acted through its duly authorized officer or other official" when terminating plaintiff's

employment, and, "based upon the Official Record as a whole, that Respondent [defendant] substantially complied with" section 4.2 governing termination "for cause." [FN30] The arbitrators expressly rejected plaintiff's argument that "somehow the failure to have official Board action" to direct that plaintiff be fired indicated a failure to terminate for cause, a breach of the employment agreement, or a lack of the "good faith" plaintiff argued was required. [FN31] The arbitrators declined *485 to award defendant attorneys' fees and costs, finding that plaintiff's claims were "unsuccessful," but not "unsupportable." [FN32]

FN30. Docket no. 6, exhibit D at 6; docket no. 1, exhibit 6 at 6.

FN31. Docket no. 6, exhibit D at 6-7 and 8; docket no. 1, exhibit 6 at 6-7 and 8.

FN32. Docket no. 6, exhibit D at 7; docket no. 1, exhibit 6 at 7

Plaintiff now seeks to vacate the arbitration award arguing, in sum, that plaintiff's employment was not terminated "for cause" in part because defendant's vice president terminated plaintiff's employment, but there was no proof the Board of Directors of defendant authorized the termination at all or before it

occurred. More specifically, plaintiff argues the arbitrators exceeded their powers by creating a new contract for the parties; engaged in misconduct under the Federal Arbitration Act ("FAA") by: revising the contract; refusing to apply Texas law; and by refusing to admit certain relevant evidence. [FN33] Defendant opposes vacating the arbitration award, arguing, in part, that the parties' arbitration provisions is a contractual waiver of the right to seek vacation of an arbitration award, an argument the Court construes as a jurisdictional challenge. [FN34]

FN33. Docket no. 1 at 2-3.

FN34. Docket no. 6 at 24. Defendants other arguments include, in part that: plaintiff has ignored the onerous standard for review of an arbitration award; plaintiff's argument that the arbitrators exceeded their authority is not supported factually or legally; even if the Board did not make the initial determination to discharge plaintiff, as required by the contract, the Board subsequently ratified the decision made by a corporate delegate; in claiming that the arbitrators engaged in a manifest disregard of Texas law, plaintiff has misconstrued the employment agreement and the applicable law; to the extent plaintiff is merely alleging that the arbitrators engaged in manifest disregard of the

facts, the allegation is not a basis for vacating the award; the parties did not stipulate to the admission of certain evidence; and plaintiff's claim that the arbitrators based their decision on evidence from a witness plaintiff was not allowed to impeach, ignores the "score of direct evidence from other witnesses and exhibits recounting plaintiff's misconduct and relied on by the Panel." *Id.* 6-24. In light of the recommendation that the Court lacks subject matter jurisdiction, it is not necessary or appropriate for the Court to reach defendant's substantive arguments, including any argument that the arbitration provision effectively waived either side's right to seek any vacation or modification of the final award based on the clause that states: "The award rendered by the arbitrators (a) shall be final, (b) shall not constitute a basis for collateral estoppel as to any issue and (c) *shall not* be subject to vacation or modification." Docket no. 6, exhibit A, appendix A at § D-10 (emphasis added).

IV. *ISSUE*

Whether the Court has subject matter jurisdiction over plaintiff's complaint to vacate the arbitration award.

V. *ARGUMENT AND ANALYSIS*

Defendant has argued that the parties, through the arbitration provision of the employment

agreement, contractually waived the right to seek to vacate or modify the arbitration award and seeks dismissal of the complaint. [FN35] Arguably, defendant's position could be construed as a challenge to the Court's subject matter jurisdiction to address the merits of plaintiff's request that the arbitration award be vacated. [FN36] Nevertheless, the Court has "a *486 duty to raise the issue of subject matter jurisdiction *sua sponte*." [FN37] Accordingly, the Court first addresses its own subject matter jurisdiction.

FN35. Docket no. 2 at 3 (dismissal is sought pursuant to Fed.R.Civ.P. 12(b)(6)); docket no. 6 at 24.

FN36. The Court notes that defendant's answer to the complaint "admits the averments contained in Paragraph II of Plaintiff's Original Complaint and that Plaintiff seeks to bring this suit for vacatur under the Federal Arbitration Act, but Defendant denies that any an all grounds for vacatur as alleged in Plaintiff's Original Complaint can be satisfied." Docket no. 2 at 2. This statement appears to be an admission that the Court has subject matter jurisdiction as alleged in Section II of the complaint. Docket no. 1 at 2. Further, defendant asserts a counterclaim of breach of contract for which defendant seeks an award of attorney's

fees and costs. Docket no. 2 at 3. By logic, the counterclaim is either premised on the same federal subject matter jurisdiction alleged in plaintiff's complaint and admitted by defendant or is intended to allege a pendent state law claim. Because this report recommends dismissal of plaintiff's complaint for want of federal subject matter jurisdiction, defendant's counterclaim should be dismissed for lack of federal subject matter jurisdiction or because the Court declines to exercise supplemental jurisdiction over the counterclaim to the extent it may be premised on state law. *See Bass v. Parkwood Hosp.,* 180 F.3d 234, 246 (5th Cir.1999) (general rule when court dismisses all federal claims before trial is "to dismiss any pendent claims," and dismissal should "expressly be without prejudice so that the plaintiff may re-file his claim in the appropriate court"); *McClelland v. Gronwaldt,* 155 F.3d 507, 520 (5th Cir.1998) (recognizing general rule and acknowledging that Supreme Court has "counseled that the dismissal of all federal claims weighs heavily in favor of declining jurisdiction;" federal court to consider "judicial economy, convenience, fairness, and comity" to decide whether to exercise jurisdiction over pendent state-law claims; "when a balance of these factors indicates that a case properly belongs in state court, as when the federal-law claims have dropped out of the lawsuit in its

early stages and only state-law claims remain, the federal court should decline the exercise of jurisdiction").

FN37. *American Heritage Life Ins. Co. v. Lang,* 321 F.3d 533, 537 (5th Cir.2003); *H & D Tire & Automotive-Hardware, Inc. v. Pitney Bowes, Inc.,* 227 F.3d 326, 328 (5th Cir.2000), *cert. denied,* 534 U.S. 894, 122 S.Ct. 214, 151 L.Ed.2d 152 (2001).

In framing the analysis of subject matter jurisdiction, the Court makes a threshold inquiry into the nature of plaintiff's claim(s). Plaintiff has initiated this case "seeking to vacate an arbitration award and for cause of action," [FN38] requesting relief solely relating to the arbitration or re-arbitration of the parties' dispute. Therefore, the "cause of action" pleaded by the complaint appears to be limited to the request to vacate the arbitration award, and not any separate cause of action, for example, for breach of contract. But, as noted, plaintiff alleges jurisdiction under section 10 of the FAA and federal question jurisdiction. To the extent plaintiff's complaint should be read as pleading a breach of contract cause of action other than seeking to vacate the arbitration award, such a claim should be dismissed on the

ground that plaintiff has not adequately pleaded or demonstrated that the Court has subject matter jurisdiction to resolve a contract dispute between two parties who reside in Texas, either under federal subject matter jurisdiction or the FAA or both.

FN38. Docket no. 1 at 1.

With respect to plaintiff's request that the arbitration award be vacated, the Court recognizes that, generally, any court's "review of an arbitration award is extraordinarily narrow." [FN39] For example, in the collective bargaining context, the United States Supreme Court has held that so long as the arbitrator's decision "draws its essence from the collective bargaining agreement" and the arbitrator is not fashioning "his own brand of industrial justice," the award cannot be set aside. [FN40] In an action to vacate an arbitration award *487 the court does not re-try matters decided by arbitration.

FN39. *Gateway Tech., Inc. v. MCI Telecommunications Corp.*, 64 F.3d 993, 996 (5th Cir.1995) (quoting *Antwine v. Prudential Bache Sec., Inc.*, 899 F.2d 410, 413 (5th Cir.1990)).

FN40. *United Paperworkers Int'l Union v. Misco, Inc.,* 484 U.S. 29, 36, 108 S.Ct. 364, 370, 98 L.Ed.2d 286 (1987) (quoting *United Steelworkers of Am. v. Enterprise Wheel & Car Corp.* 363 U.S. 593, 597, 80 S.Ct. 1358, 4 L.Ed.2d 1424 (1960)).

The parties arbitration agreement expressly provides that the arbitration provision is governed by the FAA. [FN41] Section 10 of the FAA circumscribes a court's review in a proceeding to vacate by providing that:

FN41. *See Gateway Tech., Inc.,* 64 F.3d at 997 n. 3 (when contract is silent on law governing arbitration, the FAA governs). *See also Volt Info. Sciences, Inc. v. Bd. of Trustees Leland Stanford Jr. Univ.,* 489 U.S. 468, 479, 109 S.Ct. 1248, 1256, 103 L.Ed.2d 488 (1989) ("Arbitration under the Act is a matter of consent, not coercion, and parties are generally free to structure their arbitration agreements as they see fit. Just as they may limit by contract the issues which they will arbitrate, *see Mitsubishi* [*Motors Corp. v. Soler Chrysler-Plymouth, Inc.*], *supra,* 473 U.S. [614], at 628, 105 S.Ct. [3346], at 3353, 87 L.Ed.2d 444[(1955)], so too may they specify by contract the rules under which that arbitration will be conducted.").

an award shall not be vacated unless: (1) the award was procured by corruption, fraud, or undue means; (2) there is evidence of partiality or corruption among the arbitrators; (3) the arbitrators were guilty of misconduct which prejudiced the rights of one of the parties; or (4) the arbitrators exceeded their powers. [FN42]

FN42. *Misco, Inc.*, 484 U.S. at 36, 108 S.Ct. at 370 (citing 9 U.S.C. § 10(a)(1)-(4)).

Before a court may reach these statutory bases for vacating an arbitration award governed by the FAA, however narrow, the court must have subject matter jurisdiction to resolve the dispute.

[1] Specifically in reference to a federal court's subject matter jurisdiction to decide a petition to vacate an arbitration award governed by the FAA, the United States Supreme Court has explained that:

The Arbitration Act is something of an anomaly in the field of federal-court jurisdiction. It creates a body of federal substantive law establishing an regulating the duty to honor an agreement to arbitrate, yet it does not create any independent federal-question jurisdiction under 28 U.S.C. § 1331 or otherwise.... **[T]here must be diversity of citizenship or some other**

independent basis for federal jurisdiction.... for enforcement of the Act is left in large part to the state courts. [FN43]

FN43. *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 25 n. 32, 103 S.Ct. 927, 941-42 n. 32, 74 L.Ed.2d 765 (1983) (emphasis added).

In light of the Supreme Court's explanation, several federal appeals courts have held that section 10 of the FAA, "allowing federal district courts to vacate arbitration awards, does not confer upon federal district courts subject matter jurisdiction." [FN44] Noting the United States Supreme Court in *Moses H. Cone Memorial Hospital* was analyzing sections 3 and 4 of the FAA, the United States Court of Appeals for the Second Circuit explained "it would be anomalous to conclude... that section 4 confers no jurisdiction to compel arbitration, but that section 10 confers jurisdiction to vacate an award once arbitration takes *488 place." [FN45] Accordingly, there must be an independent basis for subject matter jurisdiction before court can consider a motion to vacate an arbitration award under the FAA. [FN46] Further, when asserting a claim under section 10 in federal court, plaintiff must demonstrate that federal diversity or federal question jurisdiction exists. [FN47]

FN44. *Perpetual Sec., Inc. v. Tang,* 290 F.3d 132, 136 (2d Cir.2002); *see Baltin v. Alaron Trading Corp.,* 128 F.3d 1466, 1469 (11th Cir.1997), *cert. denied,* 525 U.S. 841, 119 S.Ct. 105, 142 L.Ed.2d 84 (1998); *Minor v. Prudential Sec., Inc.,* 94 F.3d 1103, 1104-05 (7th Cir.1996), *cert. denied,* 519 U.S. 1113, 117 S.Ct. 954, 136 L.Ed.2d 841 (1997); *Ford v. Hamilton Inv., Inc.,* 29 F.3d 255, 257 (6th Cir.1994); *Garrett v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 7 F.3d 882, 884 (9th Cir.1993); *see also Judd v. Texakoma Fin., Inc.,* No. 3:96-CV-2604- P, 1996 WL 734940, at *4 (N.D.Tex. Dec. 11, 1996) (dismissing because from face of motion to vacate "it appears that the dispute does not involve a substantial question of federal law").

FN45. *Harry Hoffman Printing, Inc. v. Graphic Communications Int'l Union, Local 261,* 912 F.2d 608, 611 n. 1 (2nd Cir.1990) (citation omitted). The Court also observed: "Further, to read section 10 as bestowing jurisdiction to vacate absolutely any arbitration award would open the federal courts to a host of arbitration disputes, an intent that we should not readily impute to Congress." *Id.*

FN46. *Perpetual Sec., Inc.,* 290 F.3d at 136; *Minor,* 94 F.3d at 1105.

FN47. *Id.*

[2] In this case, plaintiff does not allege diversity jurisdiction. [FN48] Further, there is no basis in the complaint for the Court to conclude the parties are of diverse citizenship; indeed, plaintiff's complaint alleges both parties reside in Texas. [FN49] Nor does plaintiff's complaint allege any specific amount in controversy. But, plaintiff's complaint does seek to allege federal question subject matter jurisdiction pursuant to 28 U.S.C. § 1331. [FN50] Federal question jurisdiction arises only when exists when the complaint standing alone "establishes either that federal law creates the cause of action or that the plaintiff's right to relief necessarily depends on resolution of a substantial question of federal law." ' [FN51] The federal question "must be disclosed upon the face of the complaint." [FN52]

FN48. Docket no. 1 at 1.

FN49. *Id.*

FN50. *Id.* at 1-2.

FN51. *Franchise Tax Bd. of the State of Cal. v. Construction Laborers Vacation Trust for S. Cal.,* 463 U.S. 1, 27-28, 103 S.Ct. 2841, 2856, 77 L.Ed.2d 420 (1983).

FN52. *Phillips Petroleum Co. v. Texaco, Inc.,* 415 U.S. 125, 127- 28, 94 S.Ct. 1002, 1003, 39 L.Ed.2d 209 (1974).

Plaintiff seeks to have the arbitration award vacated because the arbitrators allegedly exceeded their authority by creating a new contract for the parties and because the arbitrators "engaged in 'misconduct' under the [FAA] as the same has been interpreted by the Federal Courts by revising the agreement and by refusing to apply Texas law as required by the Arbitration provision." [FN53] Plaintiff additionally alleges that the arbitrators engaged in misconduct by refusing to admit certain relevant evidence. [FN54] These allegations do not raise a federal question. First, plaintiff has not alleged any violation of federal law. Although plaintiff alleges the arbitrators violated the FAA, as stated above, the Supreme Court and federal appeals courts have held that

such claims do not create an independent federal question. Second, plaintiff's right to relief does not depend on the "resolution of a substantial question of federal law." [FN55] Plaintiff is seeking to vacate the arbitration award based on the alleged mistakes of the arbitrators. As the Seventh Circuit has explained:

FN53. Docket no. 1 at 2.

FN54. *Id.* at 2-3.

FN55. *See Franchise Tax Bd.,* 463 U.S. at 28, 103 S.Ct. at 2856.

[A] motion to vacate on the grounds of fraud, corruption, undue means, evident partiality, and failure to consider pertinent and material evidence, does not require the resolution of any federal issue, let alone a substantial question of *489 federal law. [FN56]

FN56. *Minor,* 94 F.3d at 1105.

The Court notes that the Second Circuit acknowledged in *Perpetual Securities, Inc.* that it had elsewhere "**intimated** that an allegation

that an arbitration panel manifestly disregarded **federal** law will give rise to federal question jurisdiction." [FN57] Both plaintiff's complaint and plaintiff's other pleadings in this Court acknowledge that Texas law governs the interpretation of the employment agreement. And, as in *Perpetual Securities, Inc.*, plaintiff's "allegations cannot be the basis for subject matter jurisdiction," [FN58] in this case, because plaintiff's contentions as reflected on the face of the complaint do not demonstrate the panel's manifest disregard of federal law. Rather, plaintiff's complaint supports the conclusory allegation of "manifest disregard of the law" in reference to plaintiff's contention that the arbitrators "engaged in misconduct under the ... [FAA] ..." as same has been interpreted by the Federal Courts by revising the agreement [to allow defendant's vice-president to terminate plaintiff's employment for "the Company"] and by refusing to apply Texas law as required by the arbitration provision" and by "refusing to allow the introduction of relevant impeachment evidence." [FN59] These more specific allegations addressing interpretation of the employment agreement, Texas law, and admission of evidence do not sufficiently plead a claim of manifest disregard of federal law to give rise to federal question jurisdiction. Moreover, if the Court considers plaintiff's brief in support of the petition to vacate in assessing

federal question jurisdiction, [FN60] the brief continues to focus on the arguments, already advanced to the arbitration panel, that defendant's vice-president could not terminate plaintiff's employment "for cause" for "the Company" because there is no proof defendant's Board of Directors made the decision, plaintiff was not first called before the Board to discuss the termination, plaintiff and the President of the Board "understood" (in an apparent unwritten agreement apart from the written employment agreement) that plaintiff would be terminated only by action of the Board, [FN61] a duty of "good faith and fair dealing" recognized in Texas law should have been applied to the termination decision, and impeachment evidence should have been admitted and considered. [FN62] These arguments demonstrate plaintiff's disagreement with the final "binding arbitration decision and opinion" and desire for this Court to review plaintiff's version of the facts and the law, but not manifest disregard of federal law sufficient to confer federal question jurisdiction.

FN57. *Perpetual Sec., Inc.,* 290 F.3d at 139 (emphasis added) (citing *Greenberg v. Bear, Stearns & Co.,* 220 F.3d 22, 27 (2nd. Cir.2000), *cert. denied,* 531 U.S. 1075, 121 S.Ct. 770, 148 L.Ed.2d 669

(2001)); *see also Judd,* 1996 WL 734940, at *5 (noting that "[i]t is conceivable that [disregard of the law and public policy grounds] could involve the resolution of a substantial question of federal law" but finding that because underlying claims were based in state law, "it thus stands to reason that any law that may have been 'manifestly disregarded' or any public policy that may have been violated was state in nature.").

FN58. 290 F.3d at 139.

FN59. Docket no. 1 at 2-3.

FN60. *See Minor,* 94 F.3d at 1105 (examines the face of the motion to vacate to determine if federal question jurisdiction exists); *Judd,* 1996 WL 734940, at *5 (same).

FN61. Docket no. 5 at 3.

FN62. *E.g., id.* at 2-22.

In sum, because the Court has federal subject matter jurisdiction over a petition to vacate an

arbitration award pursuant to *490 section 10 of the FAA only when diversity of citizenship or federal question jurisdiction exists, because plaintiff has not alleged diversity jurisdiction, because plaintiff's grounds for vacating the arbitration award do not appear to require the resolution of a substantial question of federal law sufficient to accord federal question jurisdiction, the Court lacks federal subject matter jurisdiction over plaintiff's complaint. Accordingly, it is not necessary or proper for the Court otherwise to address the merits of the parties' claims.

VI. *RECOMMENDATION*

Based on the foregoing analysis, it is recommended that: plaintiff's complaint [FN63] be **DISMISSED** for lack of federal subject matter jurisdiction; and defendant's counterclaim be **DISMISSED** for lack of federal subject matter jurisdiction, or, in the alternative and to the extent a pendent state law claim may have been alleged, because the Court declines to exercise supplemental jurisdiction over the counterclaim.

FN63. Docket no. 1.

VII. *INSTRUCTIONS FOR SERVICE AND NOTICE OF RIGHT TO OBJECT/APPEAL*

The United States District Clerk shall serve a copy of this Report and Recommendation on each and every party either (1) by certified mail, return receipt requested, or (2) by facsimile if authorization to do so is on file with the Clerk. According to 28 U.S.C. § 636(b)(1) and Fed. R. Civ. P. 72(b), any party who desires to object to this report must serve and file written objections to the Report and Recommendation within 10 days after being served with a copy unless this time period is modified by the District Court. A party filing objections must specifically identify those findings, conclusions or recommendations to which objections are being made and the basis for such objections; the district court need not consider frivolous, conclusive or general objections. **Such party shall file the objections with the Clerk of the Court, and serve the objections on all other parties and the Magistrate Judge**. A party's failure to file written objections to the proposed findings, conclusions and recommendations contained in this report shall bar the party from a de novo determination by the District Court. [FN64] Additionally, any failure to file written objections to the proposed findings, conclusions and recommendations contained in this Report and Recommendation within 10 days after being served with a copy shall bar the aggrieved party, except upon grounds of plain error, from attacking on appeal the unobjected-to proposed

factual findings and legal conclusions accepted by the District Court. [FN65]

FN64. *See Thomas v. Arn,* 474 U.S. 140, 150, 106 S.Ct. 466, 472, 88 L.Ed.2d 435 (1985).

FN65. *Acuna v. Brown & Root Inc.,* 200 F.3d 335, 340 (5th Cir.2000); *Douglass v. United Serv. Auto. Ass'n,* 79 F.3d 1415, 1428 (2002).

ORDERED, SIGNED AND ENTERED this 6th day of June, 2003

PAMELA A. MATHY
UNITED STATES
MAGISTRATE JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

COLE SMITH,	§	
	§	
Plaintiff,	§	
	§	
v.	§	No. SA-02A-1022
	§	
RUSH RETAIL CLEANERS,	§	
	§	
	§	
Defendant.	§	

ORDER ACCEPTING REPORT AND RECOMMENDATION OF THE UNITED STATES MAGISTRATE JUDGE DATED JULY 1, 2003 291 F.SUPP. 2d 479

BIERY, District Judge.

Before the Court is the Report and Recommendation (docket no. 15) of the United States Magistrate Judge, plaintiff's written objections thereto (docket no. 17), and defendant's response to plaintiff's written objections (docket no. 18).

Where no party has objected to a Magistrate Judge's Report and Recommendation, the Court need not conduct a de novo review of the Report and Recommendation. *See* 28 U.S.C. § 636(b)(1) ("A judge of the court shall make a de novo determination of those portions of the report or specified proposed findings and recommendations to which objection is made."). In such cases, the Court need only review the Report and Recommendation and determine whether it is clearly erroneous or contrary to law. *United States v. Wilson,* 864 F.2d 1219, 1221 (5th Cir.), *cert. denied,* 492 U.S. 918, 109 S.Ct. 3243, 106 L.Ed.2d 590 (1989).

On the other hand, any Report and Recommendation to which objection is made requires de novo review by the Court. Such a review means that the Court will examine the entire record, and will make an independent assessment of the law. The Court need not, however, conduct a de novo review when the objections are frivolous, conclusive, or general in nature. *Battle v. United States Parole Comm'n,* 834 F.2d 419, 421 (5th Cir.1987).

The Court has thoroughly analyzed plaintiff's submission in light of the entire record. As required by Title 28 U.S.C. § 636(b)(1)(c), the Court has conducted an independent review of the entire record in this cause and has conducted

a *de novo* review with respect to those matters raised by the objections. After due consideration, the Court agrees with the Magistrate Judge's conclusion that, because the Court has federal subject matter jurisdiction over a petition to vacate an arbitration award pursuant to section 10 of the FAA only when diversity of citizenship or federal question jurisdiction exists, because plaintiff has not alleged diversity jurisdiction, and because plaintiff has not alleged that his grounds for vacating the arbitration award require the resolution of a substantial question of federal law sufficient to accord federal question jurisdiction, the Court lacks federal subject matter jurisdiction over plaintiff's complaint.

The Supreme Court cases relied upon by plaintiff in his objections are relevant to the general question of whether an arbitration clause in an employment contract is covered by the FAA. *EEOC v. Waffle House, Inc.,* 534 U.S. 279, 122 S.Ct. 754, 151 L.Ed.2d 755 (2002) (Supreme Court addressed whether an arbitration clause in an employment contract "preempted" the ability of the EEOC to file a lawsuit for discrimination seeking victim-specific relief); *Circuit City Stores, Inc. v. Adams,* 532 U.S. 105, 121 S.Ct. 1302, 149 L.Ed.2d 234 (2001) (Supreme Court addressed whether an employment discrimination case

should be dismissed pending arbitration pursuant to a clause in the employment contract). The cases do not hold that a federal court has subject matter jurisdiction over a claim for breach of an employment contract when the contract has an arbitration clause, but the plaintiff has not demonstrated either diversity or *481 federal question jurisdiction. The decision of the United States Supreme Court in *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 25 n. 32, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983), and the cases cited in the Report and Recommendation, stand for the proposition that a plaintiff must demonstrate federal question or diversity jurisdiction and that invocation of the FAA by itself will not suffice. While the FAA may be applicable to an underlying dispute, as in *Circuit City* and *Waffle House, Inc.*, it does not serve as an independent basis for jurisdiction. *See Moses H. Cone Mem'l Hosp.*, 460 U.S. at 25 n. 32, 103 S.Ct. 927.

ACCORDINGLY, IT IS THEREFORE ORDERED that the Report and Recommendation (docket no. 15) filed in this cause is ACCEPTED pursuant to 28 U.S.C. § 636(b)(1) such that plaintiff's complaint is DISMISSED for lack of federal subject matter jurisdiction; and defendant's counterclaim is DISMISSED for lack of federal subject matter

jurisdiction, or, in the alternative and to the extent a pendent state law claim may have been alleged, because the Court declines to exercise supplemental jurisdiction over the counterclaim. Motions pending with the Court, if any, are dismissed as moot. Each side is to bear its respective costs.

It is so ORDERED.

Signed this the 1st day of July 2003.

FRED BIERY
U. S. DISTRICT JUDGE

IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF TEXAS
SAN ANTONIO DIVISION

COLE SMITH,	§	
	§	
Plaintiff,	§	
	§	
v.	§	No. SA-02A-1022
	§	
RUSH RETAIL CLEANERS,	§	
	§	
Defendant.	§	

ORDER DENYING PLAINTIFF'S MOTION FOR REHEARING AND TO AMEND JUDGMENT DATED JULY 25, 2003

Before the Court is Plaintiff's Motion for Rehearing and to Amend Judgment (docket no. 22), defendant's response (docket no. 24), and plaintiff's reply (docket no. 25). After careful consideration of the motion and response, previous recommendations and orders, the pleadings on file and the entire record in this matter, the Court is of the opinion the motion should be denied.

The underlying dispute between the parties involves a claim by plaintiff against defendant for breach of an Employment Agreement, specifically whether defendant terminated plaintiff for "cause" as defined by the agreement. The Employment Agreement contains an arbitration provision requiring application of the Federal Arbitration Act ("FAA"). The parties instituted arbitration proceedings to resolve the dispute and on July 29, 2002, the arbitration panel rendered its decision in defendant's favor and denied plaintiff's wrongful discharge claim. Plaintiff filed an Original Complaint in this Court seeking to vacate the arbitration decision alleging grounds set forth in the FAA. Defendant answered in its responsive pleadings and denied that plaintiff satisfied any of the grounds for vacatur set forth in the FAA.

On June 6, 2003, United States Magistrate Judge Pamela Mathy raised the issue of federal subject matter jurisdiction under the FAA. After discussion and analysis, Judge Mathy concluded in the Report and Recommendation that, while the FAA is applicable to the arbitration proceedings mandated by the Employment Agreement between the parties, including plaintiff's subsequent complaint to vacate the arbitration decision, the FAA by itself does not grant federal subject matter

jurisdiction. Accordingly, Judge Mathy recommended the plaintiff's complaint be dismissed for lack of federal subject matter jurisdiction due to the absence of either diversity between the parties or federal question grounds. Plaintiff filed objections to the Report and Recommendation, to which defendant responded.

On July 1, 2003, this Court concluded a de nova review of the federal subject matter jurisdiction issue under the FAA and entered an order and judgment accepting the Report and Recommendation of the Magistrate Judge, also concluding that federal subject matter jurisdiction over a petition to vacate an arbitration award pursuant to the FAA exists only when diversity of citizenship or a federal question is raised. As neither diversity of citizenship nor a federal question is present in this case, this Court dismissed the case. Plaintiff now seeks to set aside the order and judgment.

The Court agrees that plaintiff alleged jurisdiction under the FAA and 28 U.S.C. §1331. The Court also agrees defendant did not challenge subject matter jurisdiction. The Court disagrees with the implication that a federal court does not have the independent responsibility to determine its own jurisdiction.

Trizec Properties, Inc. v. Unites States Mineral Prods. Co., 974 F.2d 602, 604 (5th Cir. 1992) ("Because we may not proceed with requisite jurisdiction, it is incumbent upon federal courts, trial and appellate, to examine constantly the basis of jurisdiction, so doing on our own motion if necessary."). The Court also disagrees that a Magistrate Judge is required to give advance notice before addressing subject matter jurisdiction in a Report and Recommendation to a District Judge on a pending motion. The Magistrate Judge's Report and Recommendation is the advance notice; nothing is decided until the District Judge rules. And, if the Court must determine its subject matter jurisdiction even if it is not challenged by the parties, the Court also disagrees that there is federal question jurisdiction for any federal court to review any employment dispute merely because the parties arbitrated the dispute under the FAA. See Moses H. Cone Mem'l Hosp. v. Mercy Constr. Corp., 103 S.Ct. 927 (1983).

With respect to the key cases cited by plaintiff, Southland Corp. v. Keating, 104 S.Ct. 852 (1984), addressed the question of whether the Court had jurisdiction to decide whether the FAA preempted California law voiding the arbitration, certainly a federal question; in Prima Paint Corp. v. Flood & Conklin Mfg.,

Co., 87 S.Ct. 1801 (1967) (discussed in Southland Corp., 104 S.Ct. at 865), the Court found that the FAA may be applied to diversity cases (the issue addressed was whether a federal court or an arbitrator should decide if there was fraud in the inducement of a contract and the Court determined it was an issue for the arbitrator based on the record in the case); and in Bernhardt v. Polygraphic Co. of Am., 76 S.Ct. 273 (1956) (discussed in Southland, 104 S.Ct. at 865), the Court held that the duty to arbitrate a contract dispute is outcome-determinative under Erie and, therefore, state law applies in federal diversity cases.

Both Prima Paint and Bernhardt were decided before Moses H. Cone Mem'l Hosp. v. Mercy Constr. Corp., 103 S.Ct. 927 (1983). Therein, the Court observed that the FAA creates an "anomaly" in that the FAA preempts state law and creates a body of federal substantive law, but "does not create any independent federal-question jurisdiction." Id. At 942 n. 32. The Fifth Circuit recently reiterated and applied this principle in Rio Grande Underwriters v. Pitts Farms, Inc.:

> The FAA is not an independent source of jurisdiction. A party may obtain relief in federal court under the FAA only when the

> underlying civil action would otherwise be subject to the court's federal question or diversity jurisdiction.

267 F.3d 683, 684 (5th Cir. 2001); see also Kasap v. Folger Nolan Fleming & Douglas, Inc., 166 F.3d 1243 (D.C. Cir. 1999). Given lack of federal subject matter jurisdiction in this case, plaintiff's motion is denied.

IT IS THEREFORE ORDERED that Plaintiff's Motion for Rehearing and to Amend Judgment (docket no. 22) is DENIED.

It is so ORDERED.

SIGNED this 25th day of July, 2003.

_____

FRED BIERY
UNITED STATES DISTRICT JUDGE

IN THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

NO. 03-50897
NO. 03-51005

COLE SMITH
Plaintiff – Appellant
v.
RUSH RETAIL CENTERS, INC.
Defendant – Appellee

APPEALED FROM THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF TEXAS, SAN ANTONIO DIVISION

MARCH 3, 2004 360 F.3d 504

Before HIGGINBOTHAM, DAVIS and PRADO, Circuit Judges.

PER CURIAM:

Cole Smith filed suit in the district court seeking to vacate an arbitration award entered in favor of Smith's former employer, **Rush Retail**

Centers, Inc. (Rush). Although Rush did not object to the district court's jurisdiction, a magistrate judge determined that there was no basis for federal jurisdiction because the parties were not diverse and the complaint did not allege a federal question. Over Smith's objections, the district court concurred with the magistrate judge's determination and dismissed for lack of jurisdiction both Smith's complaint and Rush's counterclaim for attorneys' fees. The court denied Smith's timely motion to amend the judgment or, alternatively, for rehearing.

***505** Smith appeals arguing that under the Federal Arbitration Act (FAA), 9 U.S.C. § 10, the district court has jurisdiction to consider his petition to vacate the arbitration award.

[1][2] Our review of the district court's determination of subject matter jurisdiction is plenary. [FN1] In relevant part, § 10 provides that "the United States court in and for the district wherein the [arbitration] award was made may make an order vacating the award upon the application of any party to the arbitration ... where the arbitrators were guilty of misconduct...." [FN2] Smith's district court complaint alleged that the arbitrators engaged in "misconduct" within the meaning of § 10(a) by revising the agreement, by refusing to apply Texas law as required by the arbitration

agreement and by refusing to allow Smith to introduce impeachment evidence.

> FN1. *Rutherford v. Harris County, Tex.,* 197 F.3d 173, 189-90 (5th Cir.1999).
>
> FN2. 9 U.S.C. § 10(a)(3) (1999).

[3] The Supreme Court has held that § 4 of the FAA, which authorizes the filing of a petition to compel arbitration in the district court, does not create an independent basis for federal jurisdiction. [FN3] Section 4 provides:

> FN3. *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.,* 460 U.S. 1, 25 n. 32, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. [FN4]

FN4. 9 U.S.C. § 4 (1999).

In short, for a federal court to enter an order to compel arbitration under § 4, "there must be diversity of citizenship or some other independent basis for federal jurisdiction before the order can issue." [FN5]

FN5. *Moses Cone,* 460 U.S. at 25 n. 32, 103 S.Ct. 927; *see also*

Prudential-Bache Sec., Inc. v. Fitch, 966 F.2d 981, 987 (5th Cir.1992) (explaining that "*Moses Cone* establishes definitively that the FAA does not provide an independent basis for federal jurisdiction").

Although *Moses Cone* arose in the context of § 4, this conclusion applies with equal force to § 10. It is well established that the FAA is not an independent grant of federal jurisdiction. Although we have not addressed whether this rule applies in the § 10 context, other circuits have. The Second, Sixth, Seventh, Ninth, Eleventh, and District of Columbia Circuits have held that § 10 of the FAA does not confer federal jurisdiction and that there must be an independent basis for federal jurisdiction before a district court may entertain a petition to vacate an arbitration award. [FN6] The Second Circuit

reasoned that "it would be anomalous to conclude ... that section 4 confers no jurisdiction to compel arbitration, but that section 10 confers jurisdiction to vacate an award once arbitration *506 takes place." [FN7] If § 10 conferred jurisdiction, "then any contract that involved commerce and contained a valid arbitration clause could give rise to a federal court action for the confirmation, vacatur, or modification of an arbitration award." [FN8] This reasoning is consistent with the limited nature of federal subject matter jurisdiction. We join our sister circuits in holding that FAA § 10 does not create federal subject matter jurisdiction.

FN6. *See Greenberg v. Bear, Stearns & Co.,* 220 F.3d 22, 25 (2d Cir.2000); *Kasap v. Folger Nolan Fleming & Douglas, Inc.,* 166 F.3d 1243, 1245-47 (D.C.Cir.1999); *Baltin v. Alaron Trading Corp.,* 128 F.3d 1466, 1469 (11th Cir.1997); *Minor v. Prudential Sec., Inc.,* 94 F.3d 1103, 1104 (7th Cir.1996); *Ford v. Hamilton Invs., Inc.,* 29 F.3d 255, 257 (6th Cir.1994); *Garrett v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,* 7 F.3d 882, 883-84 (9th Cir.1993).

FN7. *Baltin,* 128 F.3d at 1471 (quoting *Harry Hoffman Printing, Inc. v. Graphic Communications Int'l Union, Local 261,* 912 F.2d 608, 611 (2d Cir.1990)).

FN8. *Id.* (internal footnotes omitted).

We reject Smith's argument that *Circuit City Stores, Inc. v. Adams* [FN9] dictates that the arbitration of employment contracts always involves a federal question. Federal jurisdiction was not at issue in *Circuit City*. Jurisdiction was based on diversity. At issue was whether FAA § 1, which exempts from coverage under the FAA " 'contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce,' " [FN10] removes all employment contracts from the scope of the FAA or whether it merely provides that the FAA does not apply to employment contracts involving transportation workers. The Supreme Court's application of the exemption employment contracts involving the transportation industry from FAA coverage is irrelevant to the existence of federal subject matter jurisdiction under the FAA.

FN9. 532 U.S. 105, 121 S.Ct. 1302, 149 L.Ed.2d 234 (2001).

FN10. 9 U.S.C. § 1.

We conclude that the complaint did not allege a federal question or that under the facts alleged there is another basis for federal jurisdiction. We affirm the judgment dismissing the complaint.

C.A.5 (Tex.), 2004.

Supreme Court, U.S.
FILED
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No. 04-191

IN THE

Supreme Court of the United States

COLE SMITH,

Petitioner,

v.

RUSH RETAIL CENTERS, INC.,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF IN OPPOSITION

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COUNTER STATEMENT OF QUESTIONS PRESENTED

1. Does a purported "need" for a uniform national policy regulating employment arbitration agreements warrant ignoring the plain terms of the Federal Arbitration Act and further warrant overruling *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983), both of which permit concurrent jurisdiction in state and federal courts?

2. Should this Court exercise its discretionary jurisdiction to alter well-established law concerning concurrent jurisdiction under the Federal Arbitration Act when there has been no demonstrated need to do so in the last twenty years and when Congress itself has not amended the jurisdictional provisions of the Federal Arbitration Act?

3. Did this Court intend to overrule *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1 (1983), and its extensive progeny *sub silentio* in *Circuit City Stores v. Adams*, 532 U.S. 105 (2002)?

RULE 29.6 STATEMENT

Respondent Rush Retail Centers, Inc., is wholly owned by Rush Enterprises, Inc.

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STATEMENT OF THE CASE

Petitioner, Cole Smith, alleged that Respondent, Rush Retail Centers, Inc., breached an employment agreement by dismissing Smith without cause. R1:2.[1] The employment agreement contained an arbitration provision requiring application of the Federal Arbitration Act (FAA). R1:2. Consequently, the parties arbitrated their employment dispute, and the arbitration panel rendered a binding decision in Respondent's favor. R1:2, 144-52.

Petitioner then filed a complaint in the federal district court, seeking to vacate the arbitration decision. R1:2; *see also* 9 U.S.C. § 10. Petitioner alleged the district court had subject-matter jurisdiction on the basis of Section 10 of the FAA, as well as federal question jurisdiction under 28 U.S.C. § 1331. R1:2. According to Petitioner, the arbitration panel committed misconduct under the FAA and refused to apply Texas law. R1:2-3.

The district court dismissed Petitioner's claim for lack of subject-matter jurisdiction. The United States Court of Appeals for the Fifth Circuit affirmed the district court's ruling with a per curiam opinion. The lower courts held that Petitioner had not established diversity or federal question jurisdiction.

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1. The Fifth Circuit's record is cited by volume and page number.

REASONS FOR DENYING THE PETITION

I. The Underlying Decision Is Correct And Does Not Conflict With Any Prior Law.

In reaching their decisions, the lower courts followed this Court's prior opinions. In no way does the Fifth Circuit's opinion conflict with another circuit court or with any decision by a state court of last resort. The Fifth Circuit faithfully followed the rule of law. Thus, there is no reason for this Court to exercise its jurisdiction. *See* SUP. CT. R. 10(a).

The lower court decisions are based on *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 25 n.32 (1983), where this Court held that the FAA does ***not*** create "any independent federal-question jurisdiction." Before the federal courts have subject-matter jurisdiction over an FAA claim, "there must be diversity of citizenship or some other independent basis for federal jurisdiction." *Id.* The Court reiterated its *Moses H. Cone* holding in *Southland Corp. v. Keating*, 465 U.S. 1, 15 n.9 (1984).

The Fifth Circuit's decision is consistent with *Moses H. Cone* and *Southland Corp.*, and further consistent with the holdings of the other circuits. *See, e.g., Harry Hoffman Printing, Inc. v. Graphic Communications, Int'l Union, Local 261*, 912 F.2d 608, 611 (2d Cir. 1990); *Garrett v. Merrill Lynch, Pierce, Fenner & Smith*, 7 F.3d 882, 884 (9th Cir. 1993); *Ford v. Hamilton Invests., Inc.*, 29 F.3d 255, 257-58 (6th Cir. 1994); *Minor v. Prudential Sec., Inc.*, 94 F.3d 1103, 1104 (7th Cir. 1996), *cert. denied*, 519 U.S. 1113 (1997); *Baltin v. Alaron Trading Corp.*, 128 F.3d 1466, 1470-71 (11th

Cir. 1997), *cert. denied*, 525 U.S. 841 (1998); *Kasap v. Folger Nolan Fleming & Douglas, Inc.*, 166 F.3d 1243, 1246 (D.C. Cir. 1999).

The Eleventh Circuit observed it could "locate ***no*** authority disputing our conclusion that Sections 10 and 11 of the FAA do not confer subject matter jurisdiction on federal courts." *Baltin v. Alaron Trading Corp.*, 128 F.3d at 1471 n.14 (emphasis added). Likewise, Respondents here were unable to find any authority contrary to the Fifth Circuit's decision or any authority critical of the *Moses H. Cone* holding.

Because the FAA does not itself confer subject-matter jurisdiction, Petitioner was required to establish diversity of citizenship or federal-question jurisdiction. *Moses H. Cone Mem'l Hosp. v. Mercury Const. Corp.*, 460 U.S. at 25 n.32. There is no diversity in this case, and Petitioner's complaint did not allege violation of any federal law, other than the FAA.[2]

Yet Petitioner maintains, against the great weight of precedent, that invocation of the FAA ***should*** involve a substantial question of federal law sufficient to confer subject-matter jurisdiction in the federal courts. In making

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2. In FAA cases, there is some dispute among the circuits about the extent to which a federal statute, other than the FAA, should be invoked before it has raised a substantial question of federal law for purposes of conferring federal-question jurisdiction. *Compare Blue Cross of Cal. v. Anesthesia Care Assocs. Med. Group, Inc.*, 187 F.3d 1045, 1050 n.5 (9th Cir. 1999), *with Greenberg v. Bear, Stearns & Co.*, 220 F.3d 22, 25 (2d Cir. 2000), *cert. denied*, 531 U.S. 1075 (2001). Because ***no*** federal statute was invoked here (other than the FAA), this dispute is irrelevant.

this argument, Petitioner fails to mention *Moses H. Cone* or acknowledge *Southland Corp.*, decisions which are now considered hornbook law. *See, e.g.*, DANIEL P. O'MEARA, ARBITRATION OF EMPLOYMENT DISPUTES 85 (2002).

Instead, Petitioner bases his jurisdictional theory on broad language contained in *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105 (2002). That case, however, is inapposite. Subject-matter jurisdiction in *Circuit City* was based on diversity of citizenship. Petition for Writ of Certiorari (Circuit City Stores, Inc.), 2000 WL 34014993, No. 99-1379, *4 (U.S. Feb. 16, 2000). *Circuit City* addresses the FAA's exclusionary language rather than jurisdiction under the FAA. The Court held that FAA coverage does not extend to employment contracts of transportation workers, but does extend to other employment contracts affecting interstate commerce. Neither *Circuit City* (nor any other opinion) supports Petitioner's assertion that arbitration of employment contracts is a federal question for purposes of subject-matter jurisdiction.

II. Petitioner Raises No Compelling Reasons For Granting His Petition.

Review on writ of certiorari is a matter of judicial discretion, rather than of right, and a petitioner must demonstrate compelling reasons for the Court to exercise its jurisdiction. *See* SUP. CT. R. 10. Yet the Petitioner here never claims that either the district court or the Fifth Circuit deviated from the controlling legal standard. In fact, as explained *supra*, the lower courts appropriately followed this Court's holding that state and federal courts have concurrent jurisdiction under the FAA.

Rather than focus on any alleged error in the lower courts or conflict among the circuits, Petitioner claims that it is now time to change well-settled law about the FAA for the sake of a national, uniform policy regulating employment arbitration agreements — which Petitioner erroneously believes can only be accomplished if invocation of the FAA vests the federal courts with federal question jurisdiction. Petitioner, however, did not (and cannot) demonstrate that state courts have undermined the purposes of the FAA when exercising the jurisdiction left to them. Change for the sake of change is not a compelling reason for this Court to exercise its discretionary jurisdiction.

III. There Is No Important Question Of Federal Law That Should Be Settled By This Court.

Since 1983, this Court has required claims under the FAA to have an independent basis for federal jurisdiction when brought in federal district court. *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. at 25 n.32. In the last twenty years, cases have been litigated against this backdrop without any ill effect, undermining if not eliminating Petitioner's claimed need for uniformity and national policy.

Petitioner's plea for uniformity is also misplaced; it belongs in the legislative process, not the judicial process. If Congress had wanted a uniform federal approach to the arbitration of employment contracts, it could have amended the FAA long ago to provide exclusive, rather than concurrent, jurisdiction in federal courts. The congressional decision not to do so, and to maintain concurrent jurisdiction under the FAA, is entirely consistent with various other federal employment statutes that provide concurrent jurisdiction in federal and state courts. *See, e.g.*, 29 U.S.C.

§ 28(a)(2) (Fair Labor Standards Act); 29 U.S.C. § 216(b) (Family and Medical Leave Act); 29 U.S.C. § 626(c)(1) (Americans with Disabilities Act); 42 U.S.C. § 20003-5(f)(3) (Title VII of the Civil Rights Act of 1964). Contrary to Petitioner's conclusion, there is nothing inherently special about arbitration of employment disputes that elevates the FAA above any other federal statutory scheme that provides concurrent jurisdiction.

Petitioner's mere desire to make his employment contract a federal question does not make it one, nor does any case or statutory law. Petitioner has not raised any important question of federal law, and this Court should decline to exercise its jurisdiction. *See* SUP. CT. R. 10(c).

CONCLUSION

The decision of the Fifth Circuit is correct, and the Petition should be denied.

Respectfully submitted,

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